

**A. Market Power as Evidenced in CVS Company Documents, and by Actual Exercise of Market Power by CVS**

**1. The Defendants' March, 2002 Agreement and Contemporaneous Analytical Documents are Strong Evidence Both of CVS's Anticompetitive Intent and Ability to Exercise Its Market Power**

CVS company documents analyzing the market are important evidence of market structure, and strongly reinforce Plaintiff's contentions concerning the geographic and product markets, CVS's market position and entry conditions.<sup>1</sup> Defendants' anti-competitive conduct is also important evidence concerning market structure and power.<sup>2</sup> The March 2002 CVS/Anchor agreement provided for CVS's purchase of the customer prescription files of Anchor store #114 and the closing of the Anchor store. CVS store #2204 and Anchor store #114 were only .2 mile distant from one another.<sup>3</sup> At the time of the acquisition, Anchor store #114 had more prescription business than did CVS store

---

<sup>1</sup> CVS argues that documents prepared by CVS executives in the ordinary course of business are inferior as evidence to economic modeling by its hired litigation economist using a narrow subset of data. Common sense and case law suggest that reality and business persons' perceptions trump economists' models developed for litigation. As the Second Circuit explained in *Todd v. Exxon*, 275 F.3d at 205: "Industry recognition is well established as a factor that courts consider in defining a market. . . . [W]e assume that the economic actors usually have accurate perceptions of economic realities." Considering facts analogous to the instant case, the court in *Ansell Inc. v. Schmid Labs., Inc.*, 757 F. Supp. 467, 471-75 (D.N.J. 1991), noted that the defendant hired a statistics compilation company to develop data on competitors' pricing. The Court emphasized that the consultant "maintains its data separately for sales of latex condoms to U.S. retail outlets," and used this information in finding that this was an "economically distinct market segment" from the broader market for wholesale distribution of condoms." See also *Rothery Storage v. Atlas*, 792 F.2d 210, 219 n.4 (D.C. Cir. 1986); *Federal Trade Commission v. Staples, Inc.*, 970 F. Supp. 1066 (D.D.C. 1997) (where the Court relied heavily on Defendants' market documents to find an office superstores product market despite the fact that many non-superstore outlets sold the same products).

<sup>2</sup> Plaintiff's position is that Defendants' March 2002 agreement for a CVS "file-buy" from the Anchor Pharmacy in the Palisades neighborhood involved egregious anticompetitive behavior – a naked restraint of trade – that should be judged using abbreviated *per se* or truncated rule of reason ("quick look") analysis. As explained elsewhere, the CVS/Anchor agreement did not involve CVS acquisition of significant hard assets, or a business integration leading to some new product, an increase in efficiency, or new customers. In essence, CVS and Anchor agreed that CVS would pay a "premium" for market power, so that Anchor would pull its business out of the neighborhood, leaving the local pharmacy business to CVS. See Plaintiff's Motion for Partial Summary Judgment filed Aug. 2, 2004.

#2204.<sup>4</sup> The language of the agreement was specifically aimed at eliminating competition between Anchor and CVS in the Palisades neighborhood.<sup>5</sup>

The March, 2002 CVS/Anchor file buy agreement, and contemporaneous analyses of CVS company executives, make it clear that CVS believed that it could

Elimination of Anchor as a rival and the virtual purchase of Anchor's customers was the rationale for the transaction. The acquired Anchor prescription files had value to CVS only to the extent that they transferred Anchor's position in the local market.

then the value of the files to CVS would also have been trivial.<sup>6</sup>

CVS executives analyzed the expected financial consequences of the Anchor acquisition, and explained in CVS internal documents that CVS anticipated

The documents do not mention any benefit to CVS from business integration or development of better products or services.<sup>7</sup>

---

4

5

6

7

The March, 2002 CVS/Anchor file buy agreement and contemporary CVS analytical documents reflect a sophisticated understanding of local market structure by CVS executives. CVS executives believed that CVS could retain the great bulk of local Anchor pharmacy customers, which reflects a CVS analysis that the local Anchor customers had few alternatives. In other words, the documents are evidence that CVS believed it was buying market power.

The evidentiary weight of the 2002 CVS retention projections for CVS store #2204 is not seriously undermined by the fact, emphasized by CVS counsel, that some customers chose to shop elsewhere after March, 2002.<sup>8</sup>

The effective price rise is one obvious explanation for the actual loss of customers exceeding the customer loss estimates of CVS executives in 2002.<sup>10</sup>

---

<sup>8</sup> CVS and its retained expert, Dr. Harris, say that the CVS executives were befuddled in March, 2002, and not perfectly prophetic concerning retention of Anchor customers. CVS would improperly ignore the market perceptions of the CVS executives. See Harris Report at paragraph 106.

<sup>9</sup> The evidence indicates that the effect of the quality decrease is much more severe than the a "small but significant and nontransitory" increase in price referred to in part 1.11 of the FTC/USDOJ Merger Guidelines. Even if the price equivalent of the quality decline were yet greater, and the loss of customers greater, reflecting questionable judgment by CVS managers with regard to achieving customer satisfaction, that does not affect the validity of the initial projections by CVS executives,

## **2. Evidence of CVS's Assessment of CVS Store #2204's Power over Price**

Further evidence of market structure and CVS market power is found in CVS documents concerning pricing to cash customers.

risking an unprofitable loss of customers to a competitor? (Cash customers are about % of all pharmaceutical customers at CVS store #2204.<sup>13</sup>)

---

<sup>11</sup> As used in this Memorandum, “dynamic” means sensitive to potential change.

<sup>12</sup> As used in this Memorandum, “cash customers” means customers who pay for pharmaceuticals themselves rather than through insurance or government programs.

<sup>13</sup> “

<sup>17</sup> In a standard CVS price zone, prices are determined simply by adding a fixed mark-up over cost, without reacting to either relatively high or relatively low pricing by competitors, a practice that in itself reflects market power. Mr. Shea referred to it as a “default” price zone. Shea deposition, at 108.

This suggests that, following the Anchor file-buy, CVS viewed the sole price-constraining competitor to CVS store #2204 as having been removed – just as planned.

Data received from Rite-Aid confirm that CVS store #2204 and Rite Aid store #3873 are not close competitors.

### **3. Evidence of Actual Exercise of Market Power by CVS**

---

<sup>19</sup> CVS submitted Dr. Harris's affidavit in support of its motion, and the only facts he swears to concern pharmacies he says are less than 2 miles or 3 miles from CVS # 2204. His view of distance exalts abstraction over reality, in that straight line distances are used. Straight line distances would be useful only if customers could travel in a straight line, like birds. Use of the commercial Mapquest service shows that in the world of reality at least one pharmacy that Dr. Harris says is 2 miles away is actually more than 3 miles away for real world customers who use automobiles or sidewalks, and that Dr. Harris's distance calculations generally fail to match real travel distances.

Plaintiff offers evidence that CVS has already effectively raised prices for pharmaceutical products at CVS store #2204 following the CVS/Anchor transaction. That evidence demonstrates only part of CVS's potential power to raise price and reduce quality, but it is a telling demonstration of exercise of market power that is sufficient to defeat CVS's motion for summary judgment. As explained in *Todd*, 275 F.3d at 206, "[i]f a plaintiff can show that a defendant's conduct exerted an actual adverse effect on competition, this is a strong indicator of market power."<sup>20</sup>

---

<sup>20</sup> See also *Tops Mkts., Inc. v. Quality Mkts., Inc.*, 142 F.3d 90, 98 (2d Cir. 1998) (stating that market power "may be proven directly by evidence of the control of prices . . . or it may be inferred from one firm's large percentage share of the relevant market"); *Toys "R" Us*, 221 F.3d at 937 (stating that market power may be proven "through direct evidence of anticompetitive effects" or "by proving relevant product and geographic markets and by showing that the defendant's share exceeds whatever threshold is important for the practice in the case")

---

<sup>22</sup> Shea deposition, *ibid.*

<sup>23</sup> First Gaier deposition at 69-72.

<sup>24</sup> See the Goldstone deposition at 148-149.

---

<sup>25</sup> See the Reardon deposition at 17-20. Also see CVS customer feedback reports,

<sup>26</sup> See the deposition of Ronnie Pope at 35-36, 42. Mr. Pope was the District Manager in charge of CVS store #2204.

<sup>27</sup> Id. at 47-50. Also see CVS customer feedback report,

<sup>28</sup> “

<sup>29</sup>

<sup>30</sup> Reardon Deposition at 15.

---

<sup>31</sup> See, for example, CVS 079789.

<sup>32</sup> Pope deposition at 36.

<sup>33</sup> Pope deposition at 35-36, 42.

<sup>34</sup> Through August, 2003.

<sup>35</sup>

---

and indicates exercise of market power. See *Todd v. Exxon Corp.* and other cases cited earlier.

In short, the evidence of CVS's post-transaction exercises of market power support a finding that the company had market power and the ability to exercise it. Of course, for purposes of CVS's summary judgment motion it suffices for Plaintiff to point out that the evidence of exercise of market power raises issues requiring trial. To support its motion for summary judgment, it is not sufficient for CVS to argue against Plaintiff's evidence of actual anti-competitive effects. Neither can CVS argue that the relevant CVS company data on is unpersuasive because it is too small in amount, included too few transactions, sampled too few customers, or does not provide a quantifiable quality/discount adjusted price actually paid by consumers.<sup>39</sup> That Plaintiff disagrees with CVS's view of the weight to be accorded this evidence highlights that the facts and their significance are in dispute, and are ripe for a trial on the merits. In the summary judgment context a court construes all facts in the light most favorable to the nonmoving party and draws all inferences in favor of that party. See *Anderson v. Liberty Lobby, Inc.*, 477 U.S. at 255. Here, that principle requires

---

<sup>39</sup> All of these arguments were implied during CVS's deposition of Plaintiff's economic expert, Dr. Gaier.

that the Court accept that Plaintiff's evidence is a strong indicator that CVS possesses substantial market power.